

## Message Text

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ACTION ARA-20

INFO OCT-01 ADP-00 AID-20 EB-11 NSC-10 RSC-01 CIEP-02

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FM AMEMBASSY SAN SALVADOR

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INFO AMEMBASSY GUATEMALA

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E.O. 11652 - N/A

TAGS: EFIN, ES

SUBJECT: NEW MONETARY COUNCIL AND CENTRAL BANK AUTONOMY

GUATEMALA ALSO FOR ROCAP

1. SUMMARY: WITHOUT PRIOR CONSIDERATION OR DEBATE, THE LEGISLATIVE ASSEMBLY HASTILY APPROVED A LAW, ON AUGUST 23, CREATING A MONETARY COUNCIL HEADED BY THE PRESIDENT AND COMPOSED OF FIVE OTHER GOES AGENCY HEADS. THE LAW IN ESSENCE TRANSFERS ALL PREVIOUS CENTRAL RESERVE BANK (BCR) POLICY-MAKING AUTHORITY TO THE COUNCIL AND

PLACES THE BANK SUPERINTENDENCY UNDER THE COUNCIL'S DIRECTION. THE GOVERNMENT'S OBJECTIVE WAS DESCRIBED AS BEING TO MAKE THE MONETARY

POLICY AND THE BANKING SYSTEM RESPONSIVE TO THE COUNTRY'S ECONOMIC AND DEVELOPMENTAL NEEDS. THE MINISTER OF ECONOMY'S TRANSMITTAL MESSAGE TO THE ASSEMBLY CHARACTERIZED THE COUNCIL AS THE NEXT STEP IN A CONSTITUTIONAL PROGRESSION TO MODERNIZE THE MONETARY

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POLICY. THE SALVADORAN BANKERS' ASSOCIATION MET AUGUST 27, LAMENTED WHAT THEY CALLED "THIS UNCONSTITUTIONAL" ATTACK ON THE BANKS, AND AGREED TO MAKE A DETAILED ANALYSIS OF THE LAW AND PRESENT A PROTEST TO THE GOES. NEWSPAPERS HAVE BEEN RATHER

MUTE EXCEPT TO REPORT THE COMMENTS OF OPPOSITION DEPUTIES TO THE GOES' RAMMING THROUGH THE LEGISLATION IN JUST A COUPLE OF HOURS. THE PRINCIPAL EFFECTS OF THE COUNCIL ARE TO END BCR AUTONOMY, EXCLUDE DIRECT PRIVATE SECTOR INPUT INTO MONETARY POLICY ORMULATION, INVOLVE THE PRINCIPAL PUBLIC ECONOMIC POLICY OFFICIALS IN MONETARY POLICY, AND PROVIDE THE GOVERNMENT WITH DIRECT LEVERAGE OVER ALL CLIENT SECTORS OF THE BANKING SYSTEM. END SUMMARY.

2. EARLY AUGUST 23, THE LEGISLATIVE ASSEMBLY UNEXPECTEDLY TOOK UP A SURPRISE GOES-SPONSORED BILL TO CREATE A MONETARY COUNCIL (JUNTA MONETARIA). THE BILL (COPY POUCHED DEPARTMENT AND ROCAP) WAS PRESENTED BY ECONOMIC MINISTER SANCHEZ AGUILLON WHO REQUESTED URGENT ACTION. AFTER AN HOUR AND A HALF RECESS FOR COMMITTEE CONSIDERATION, THE GOVERNMENT-CONTROLLED LEGISLATURE RECONVENED AND PASSED THE BILL. IT TAKES EFFECT WITHIN SEVERAL WEEKS WHEN THE AUGUST 23 EDITION OF THE DARIO OFICIAL IS PUBLISHED. MOST NEWSPAPER REPORTS FOCUSED ON THE SUBSTANCE OF THE LAW AND COMMENTED ON THE INCREASINGLY FREQUENT RAMMING OF SIGNIFICANT MEASURES THROUGH THE SUBSERVIENT ASSEMBLY. THE ONLY EDITORIAL TREATMENT TO DATE HAS BEEN RATHER BLAND, REFERRING TO THE POSITIVE ROLE THE COUNCIL COULD HAVE AND SUGGESTING THAT THE GOVERNMENT SHOULD MAKE AMPLY CLEAR THAT THE INTENTIONS OF THE COUNCIL ARE. IT OBSERVED THAT WITH THE PRESIDENT OF THE REPUBLIC PRESIDING OVER THE COUNCIL IT LEAVES NO RECOURSE FOR APPEAL OF DECISIONS PREVIOUSLY MADE BY THE BCR; AND THAT THE BCR, ENDING AN HONORABLE CHAPTER IN THE COUNTRY'S MONETARY DEVELOPMENT, IS NOW IN A SENSE A BANK AMONG BANKS. THE BANKING COMMUNITY SWEARS IT WAS TAKEN COMPLETELY BY SURPRISE BY THE LAW AS DO OUR CONTACTS IN THE BCR. ITS DRAFTING WAS EVIDENTLY ACCOMPLISHED WITHIN THE INNERMOST CIRCLE OF THE GOVERNMENT.

3. BESIDE THE PRESIDENT OF THE REPUBLIC AS CHAIRMAN AND THE PRESIDENT OF THE BCR AS SECRETARY, THE COUNCIL'S OTHER MEMBERS ARE THE EXECUTIVE SECRETARY OF THE PLANNING OFFICE (CONAPLAN) AND THE MINISTERS OF ECONOMY, FINANCE AND AGRICULTURE. THE LIMITED OFFICIAL USE  
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DEPUTY OF EACH OF THESE OFFICIALS IS THE AUTHORIZED ALTERNATE. THE COUNCIL MAY APPOINT ITS OWN STAFF, IF IT DESIRES, TO BE PAID BY THE BCR. (WE HAVE NO INDICATION OF ANY STAFF BEING RECRUITED FOR THE COUNCIL.) THE LAW GIVES THE COUNCIL ALL POLICY AUTHORITY PREVIOUSLY HELD BY THE BCR AND PROVIDES FOR APPROPRIATE MODIFICATION OF THE BCR'S "ORGANIC LAW" TO REFLECT THE TRANSFER OF POWERS TO THE COUNCIL. THE SUPERINTENDENCY OF BANKS IS SPECIFICALLY REMOVED FROM THE JURISDICTION OF THE BCR AND PLACED UNDER THE DIRECTION OF THE COUNCIL. HENCE, THE CHIEF DOMESTIC MONETARY TOOLS -- REQUIRED BANK RESERVES, INTEREST RATE LEVELS, MONEY SUPPLY, CREDIT GROWTH AND CONTRACTION -- PLUS POLICY DECISIONS IN THE

INTERNATIONAL SPHERE-- MAGNITUDE AND COMPOSITION OF FOREIGN EXCHANGE HOLDINGS, PAR VALUES, USE OF IMF, ETC. -- PASS TO THE COUNCIL FROM THE BCR. BOTH THE ECONOMIC MINISTER SANCHEZ AND PRESIDENT MOLINA EXPLAINED THAT THE COUNCIL WAS CREATED SO THAT THE HIGH OFFICIALS WITH A POLITICAL MANDATE COULD FORMULATE POLICY TO DETERMINE THE DIRECTION AND TERMS OF CREDIT FLOWS WITHIN THE ECONOMY.

4. WHILE THE ASSEMBLY WAS CONSIDERING THE BILL, PRESIDENT MOLINA HELD A SERIES OF MEETINGS WITH VARIOUS SECTOR REPRESENTATIVES AND MERELY ANNOUNCED THE COUNCIL AS FACT. AT THE SESSION WITH THE BANKERS ASSOCIATION, ROBERTO HILL, PRESIDENT OF THE BANCO CUSCATLAN, THE MOST AGGRESSIVE SALVADORAN BANK, ASKED IF REPRESENTATION FROM THE PRIVATE SECTOR ON THE COUNCIL HAS BEEN CONSIDERED; THE PRESIDENT SAID "NO". BEFORE ANOTHER BANKER HAD COMPLETED HIS QUESTION ON WHETHER THE GOVERNMENT WOULD CONSULT WITH BANKERS BEFORE THE FACT IN ANY FUTURE LEGISLATION AFFECTING BANKS, THE PRESIDENT ABRUPTLY LEFT THE SESSION. IN THEIR MEETING AUGUST 27, THE BANKERS ASSOCIATION CRITICIZED THE LAW AND SOME PREDICTED THAT IT WAS ONLY A PRELUDE TO FULL BANK NATIONALIZATION. A FOUR-MAN COMMITTEE WAS FORMED TO WRITE A CRITIQUE WHICH WILL BE SENT TO THE PRESIDENT. FIRST NATIONAL CITY BANK'S VICE PRESIDENT, IVAN CULBERTSON, TOLD US HIS BANK IS ALREADY VERY VULNERABLE AS A FOREIGN BANK AND HE IS LOOKING FOR A WAY OF KEEPING ALL COMMUNICATION IN THE NAME OF THE ASSOCIATION RATHER THAN OVER INDIVIDUAL BANK MEMBERS' SIGNATURES. FOR HIS OWN PART, HE IS NOT UNDULY DISTURBED BY THE LAW, SEEING IT AS MUCH THE SAME POLICY BASE AS ALREADY EXISTS AND OPERATES WELL IN LIMITED OFFICIAL USE  
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SOME OTHER LATIN COUNTRIES.

5. CULBERTSON ALSO TOLD US THAT ING. JAUREGUI, THE PREDECESSOR TO THE CURRENT HEAD OF CONAPLAN, SAID THE LAW WAS IN THE WORKS WHILE HE WAS IN CONAPLAN, WHICH WOULD BE OVER A YEAR AGO. IT IS HARDLY POSSIBLE, THEREFORE, THAT BCR PRESIDENT SUAREZ WAS UNAWARE OF IT NOR EXCLUDED FROM PERTINENT CONSULTATION. (SKREZ' ABSENCE FROM THE COUNTRY WHILE THE BILL WAS PASSED RAISED SPECULATION AS TO HIS FUTURE). JAUREGUI REPORTEDLY SAID THAT THE LACK OF SUFFICIENT PUBLIC SECTOR (E.G. MINISTER OF ECONOMY IN PARTICULAR) INFLUENCE IN MONETARY POLICY HAD LED TO THE ENACTMENT OF THE LAW. (NOTE: THE HEAD OF CONAPLAN HAS ALWAYS BEEN ON THE BCR BOARD OF DIRECTORS.)

. INITIAL PRIVATE REACTIONS WERE ALMOST ALL ADVERSE TO THE LAW. THERE WERE REPORTS THAT THE PRIVATE SECTOR MEMBERS OF THE BCR BOARD OF DIRECTORS WOULD RESIGN AS MIGHT SEVERAL OF THE BCR'S SENIOR OFFICIALS. NONE OF THESE MOVES HAS MATERIALIZED AS YET AND CALMER OPINION SEVERAL DAYS LATER RIGHTLY POINTED OUT THAT THE BCR WOULD CONTINUE TO BE THE SOURCE OF

MAJOR INPUT INTO THE COUNCIL. NOT ONLY BECAUSE IT IS THE IMPLEMENTOR OF COUNCIL POLICY AND HAS THE ONLY ADEQUATE ANALYTICAL STAFF, BUT BECAUSE ITS PRESIDENT IS THE COUNCIL'S SECRETARY AND, AS SUCH, CAN CALL MEETINGS AND WILL NO DOUBT PREPARE AGENDA AND BACKUP INFORMATION.

7. COMMENT: THE GOVERNMENT'S TACTIC OF ORDERING HASTY ADOPTION OF THIS MAJOR LAW WITHOUT OUTSIDE CONSULTATIONS OR LEGISLATIVE STUDY AND DEBATE PRODUCED MUCH OF THE INITIAL AND EXTREME CRITICISM. THE GOES NO DOUBT WAS INFLUENCED IN TAKING THIS TACTIC FROM THE HARD KNOCKS THE SANCHEZ GOVERNMENT RECEIVED OVER THE LAST BANKING LAW WHEN LENGTHY DELIBERATIONS PROVIDED OPPORTUNITY FOR CONSERVATIVE FORCES TO MOUNT A RATHER EFFECTIVE CAMPAIGN OF OPPOSITION. THE EFFECTS OF THE LAW INCLUDE: 1) LOSS OF AUTONOMY OF THE CENTRAL BANK, 2) LOSS OF DIRECT REPRESENTATION BY PRIVATE SECTOR AND BANKING REPRESENTATIVES IN THE MONETARY POLICY ORGAN (THEIR REPRESENTATION ON THE BCR'S BOARD WILL GIVEN THEM ONLY AN INDIRECT VOICE, 3) DIRECT PARTICIPATION AT THE POLITICAL LEVEL OF THE CHIEF ECONOMIC POLICY ARCHITECTS IN DETERMINING THE CRITERIA AND LEVELS OF FINANCIAL RESOURCE ALLOCATION THROUGH THE BANKING SYSTEM, LIMITED OFFICIAL USE  
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4) POTENTIAL GOVERNMENT LEVERAGE OVER ALL SECTORS OF THE ECONOMY TO GAIN COOPERATION OR PREVENT OPPOSITION IN EFFECTING ANY OTHER ECONOMIC GOAL. FOR EXAMPLE, THE GOES COULD USE ITS AUTHORITY IN THE COUNCIL TO THROTTLE OPPOSITION FROM LARGE AGRICULTURAL INTERESTS TO AN AGRARIAN REFORM LAW. AN OBVIOUS PRIVATE SECTOR CONCERN SHARED BY US IS THAT THE COUNCIL WILL SACRIFICE THE PRESENT STABILIZING MONETARY POLICIES IN ORDER DEVELOPMENTAL NEEDS." HOWEVER, THE CURRENT INCUMBENTS ON THE COUNCIL ARE NOT CONSIDERED, EVEN IN THE MOST CONSERVATIVE CIRCLES, A BUNCH OF WILD-EYED LIBERALS. BOTH FINANCE MINISTER GAVIDCA AND BCR'S SUAREZ ARE IDENTIFIED WITH CAUTIOUS MONETARY AND FISCAL POLICIES. POLITICALLY, THIS MOVE IS VERY MUCH IN KEEPING WITH THE SUBSTANCE AND STYLE OF THE MOLINA ADMINISTRATION - MOVING ALTERNATELY AGAINST THE RIGHT OR THE LEFT IN A STRATEGY OF BLANCE WHEN HE FEELS THAT THESE FORCES ARE IMPEDING HIS PLANS OR LIMITING HIS ABILITY TO GOVERN. INTERESTINGLY, THE MONETARY COUNCIL LEGISLATION COMES ON THE HEELS OF THE DEPORTATION OF COMMUNIST PARTY SECRETARY GENERAL SHAFIK HANDAL (NO DOUBT APPLAUDED BY THE RIGHT) AND RUMORS ARE NOW CURRENT THAT THE PRESIDENT MIGHT NEXT FREE FOREIGN EXCHANGE PURCHASE LIMITATION TO SOFETEN THE IMPACT OF HIS LATEST MOVE AGAINST THE INTERESTS OF THE PRIVATE SECTOR. IT ALSO SUPPORTS OUR THESIS PRESENTED IN OUR A-94 :9,- CERNING THE ROLE OF THE SALVADORAN OLIGARCHY THAT THE WEALTHY CONSERVATIVES SIMPLY DO NOT HAVE THE POLITICAL LEVERAGE SIGNIFICANTLY TO INFLUENCE THE ADMINISTRATION'S COURSES OF ACTION.  
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